

Psychological Bias of Chinese Investors Due to Overconfidence- Take “Tik-Tok” for Example

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Abstract. In many cases we've found that when a company CEO is overconfident, it has a major impact on decision making, and often puts a company's future at risk. Through a modern case study in such overconfidence, I examine the causes of psychological overconfidence in its various forms. The case of Tik-Tok allows us to look at the moderating impact of overconfidence bias and decision-making by investors. We learn that prudence and indeed fear of making mistakes are reasons for successful investment.

Keywords: Overconfidence; Tik-Tok; Psychological bias.

1. Introduction

Recently short video anchors have exploded, and with them the profits of their "we media" companies in China. Investors see high profits and rush to join the business. They enter a market of short video endorsements, creation commissions, merchandising and so on. They are often not qualified for it. The profits are seductive in "we media", but success is elusive. Very few have learned its formula of success, much less found the unique actors and creators attuned to this moment. Large numbers of niche investors are losing profits and failing, and that creates its own psychological bias. They do not blame their choice of investment for the problem, but the platform itself. This, I argue, is caused by investor overconfidence and the boom in market feedback.

2. Analysis of investors' overconfidence bias in Tik-Tok

2.1 Fundamentals of behavioral finance: Overconfidence bias

Overconfidence bias is having too high an opinion of and trust in one's own judgments when making decisions or investments. These investors often lack sufficient investment analysis skills. Behavioral finance calls this 'overconfidence bias'. There are four common types of bias: "Over Ranking, the Illusion of Control, Timing Optimism, and Desirability Effect." [2] With 'Over Ranking' a person thinks his or her ability better than others when they are not as judged by actual performance. 'Illusion of Control' is the confidence that people show when they think they are in Control of a situation, but are not. They also tend to blame other people for their failures. 'Timing Optimism' is when people are overconfident about the time left to get a job done. The 'Desirability Effect' is when people overestimate the odds of something happening simply because the outcome is desirable, otherwise known as "wishful thinking". These examples of overconfidence make an analysis of this kind more precise.

"Most people overestimate their skills, whether it's changing jobs or managing assets." [1] Despite its clear dangers in decision making, overconfidence is common. "Consider, for example, that about 73% of Americans think they're better than the average driver, according to a survey by AAA." [1] When you add the rewards that sometimes come with risky behavior in business, the temptation to trust what your own feelings are telling you are hard to resist. And those feelings are often ready to ignore basic business sense. That tells you to understand the trends of the financial market, to calculate the risk coefficients according to actual situations, and to choose investments on reasonable grounds, whatever the passions of the moment. Overconfidence bias causes investors to rely on their own intuitions and to ignore facts, calculated data and expert advice. Such investors are caught in the vortex of feeling associated with a trending and hyped success. It is a recipe for failure.

2.2 Introduction of Tik-Tok

“Tik-Tok is a well-known short video app on social media. It is a short-form video hosting service owned by Chinese company ByteDance. It hosts a variety of short-form user videos, from genres like pranks, stunts, tricks, jokes, dance, and entertainment with duration from 15 seconds to ten minutes. Tik-Tok is an international version of Douyin, which was originally released in the Chinese market in September 2016. Tik-Tok was launched in 2017 for iOS and Android in most markets outside of mainland China.”[3]

The company has won first place in the download list of app stores in many countries. Its operational strategy is to conduct classified operations and management according to different operating conditions and user preferences by region. Managers need not only to collect user data but to obtain feedback and suggestions from them and operators through assessment and questions and answers. It focuses its strategy country by country, region by region. It answers to the peculiarities of culture, especially of the young who are driven by the passions of the moment, by the viral memes that suddenly appear, and then fade as quickly. Tik-Tok has learned to operationalize just this moment, which allows it to give a better user experience to very distinct groups of people, in their own moment of heightened experience. It is no surprise therefore that it is deeply loved by its users. In the United States in 2020, according to the official data of the app store, Tik-Tok won first place in the list of the most popular apps, with a praise rate of 88%. Its huge profit and future development space are naturally very attractive to investors. Short videos have become the main entertainment mode for people.[4]

The paradox is that the passions of the clients must not be equally shared by the business men and women who are trying to profit from it.

2.3 The current situation of investors who invested in Tik-Tok Commodities

Many companies have joined the Tik-Tok platform to sell their goods. It has 800 million users worldwide, and 150 million active users in China. The developmental prospects in this country are very good, and so is the constructed virtual space it has created on the internet. It is a platform designed for the imagination, both of the user, but also of the businesses who know how to elicit it. It is already one of the most profitable businesses in China, allowing many of its users, with their short videos, to earn money, and lots of it. It has little competition, having replaced Facebook, and Instagram as the platform of choice for the most motivated market, Youth. Dazzled by huge earning figures and excited by the gains already made by investors who have seemingly come from nowhere, the temptations to risk big are hard to resist.

In China, there are many who lack the capital to take big risks but are still willing to risk all to make money through the short video industry. They want to become "netizens" and to own "we media companies". They tend to have a herd mentality, because it is the same mentality that Tik-Tok tries to identify in its users. They believe that they can make money quickly, as they've seen others do. They borrow heavily and go into their own savings. And they do this without a serious consideration of their skills, or lack of them. What they don't see clearly is that the business is extremely competitive, and it screens out foolish entrepreneurs quickly. There are one a few, very few, online celebrities and investors who can successfully profit from Tik-Tok.

These investors fail for two essential reasons. They look at the immediate situation and make rash decisions. The ones who survive, who make money in this market, are 'survivors'. They have the mental strength of will to face facts, to make changes as they arise, to tear down what doesn't work and focus on what does. The others, the "losers" as will be shown, are overconfident. They've lost the ability to judge rationally. They invest blindly and without carefully analyzing the rationale for profits and opportunity costs. They lose out on actual opportunities, that follows whims. They get seduced by hyped up packaging and are led to failure when no one is fooled.

2.4 Real world case analysis

A recent case of Tik-Tok Partners was made public by an employee. The central figure, Lang Weixian, an Internet star in China, has only been a netizen for two years. Thanks to the rapid development of the Internet and the help of his boss, he became one of the most famous internet stars in the country. Alas he was greedy. He wanted to develop beyond his boss's company. He wanted company shares and funds transferred to his own name and tried to blackmail his boss to earn more money for him through contacting well known entrepreneurs. His reputation and wealth only made him more greedy and proud. He was dissatisfied with working under his boss's company and joined friends to steal his employees. He took advantage of the difference between interests to turn the boss's company into a shell company, and press it without labor. His image of dressing up stylishly and his label of "big stomach king" won favor with many investors. But, without knowing long-term operation and company management skill, the company gradually disintegrated. His blind overconfidence in his own abilities made his failure inevitable.

Because of money and fame, he developed a 'timing optimization' bias. After becoming an Internet star, he lost himself and developed hubris. He became greedy for more money and reputation. While enjoying some success, he also lost sight of the warnings of a looming crisis. He could make money as an Internet star, but not as a manager of an enterprise. The desirability effect has shaped Weixian's thinking. Praise and recognition on the Internet make him think he was capable in his worldviews. His overconfidence was insufficient to meet the challenge of breaking away from the original company and setting up his own business. Within two months, his company started to break apart.

2.5 Conclusion

Many people deceive themselves because of overconfidence bias and believe that they can earn money from the market through making high-risk bets. This bias exists in everyone's life, but many can also control it. This investigation suggests that there are several ways to help people from being affected by overconfidence bias. They can listen to other people's opinions, and learn to take their perspectives. This supports greater objectivity in decision making. They can also take a longer term perspective on their decisions. Success should not be expected immediately! An enterprise must run continuously over a long period and that requires a mature mindset. One must be ready for the unexpected that inevitably comes with developing successful companies in any field.

Exaggerating your own abilities will usually be cause for failure. one fail in investment, and cause some unnecessary troubles and more. This is the main reason why some investors fail in investment due to overconfidence.

According to previous surveys, people who are more modest and cautious can avoid more problems when investing than those who are overconfident.

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